DR. BARBERA: Thank you for the opportunity to provide some insights on trade. From my perspective, the U.S. Fed and the U.S. consumer deserve medals for their performance over the 1998-1999 period. Asia's collapse could well have triggered a global deflationary bust, but for the timely and aggressive ease of the U.S. Fed and the unrelenting spending by U.S. households, both this year and last. You can frame both the Fed's actions and the actions of U.S. consumers as enlightened surrender of a Goldilocks growth rate for the U.S. economy in order to preserve a Goldilocks growth rate for the globe.

The spectacular surge in the U.S. trade deficit registered over the past two years, viewed in this light, is the price the U.S. paid for taking responsibility for the global economy. Going forward, the newly emerging reality of rest of world recovery ends the need for U.S. booming spending and the U.S. would be wise to steer a course aimed at slowing U.S. deficit growth, given the large and rapidly growing need for foreign capital inflows to finance this imbalance.

This year's Fed tightening which is likely to continue next year, in concert with higher import prices and consequent slow real wage gains, all point to a slower trajectory for U.S. spending next year, and a substantially slower spending trajectory will stem the growth for the U.S. deficit in the year 2000.

I think with intelligent Fed policy and a bit of luck, the U.S. can slow its spending pace, stabilize its external imbalance and return to what was at the time appreciated as a Goldilocks real economy backdrop.

As to the creation of this deficit in more detail over the last several years, I think if you step back and you look at the middle 1990s, the U.S. external deficit was relatively stable. It was about 1 percent of GDP and it was harmless from a macroeconomic standpoint. Moreover, from the macro backdrop, things were nearly ideal. We had firm U.S. output growth, ample job growth and a falling rate of inflation. The U.S. industrial age corporations had regained reasonably competitive global positions and technology companies emerged as the world's preeminent players. So despite a small external imbalance on most fronts you could say that we were quite competitive globally and that trade liberalization, in fact, had been a very good thing.

Over the past two years, however, a benign U.S. trade deficit has been replaced by a large and rapidly growing external imbalance. As of the third quarter of this year, the net export imbalance stood at 3 percent of GDP. In real terms, net export deficit was 3.8 percent of GDP, eclipsing the 3 percent mid-1980s record by a wide margin.

What happened? Prices abroad generated a number of violent economic waves which worked together to drive deficits into record-breaking territory. I think to nobody's surprise, U.S. exports to collapsing emerging Asian countries fell precipitously in 1997 and throughout 1998. As a consequence, U.S. export growth slowed to a near standstill.

Somewhat more surprising, certainly at the outset, was what happened on the import side of the ledger. Collapsing Asian economies lost access to global capital markets. Capital raced back to the U.S. and this drove U.S. long-term interest rates sharply lower. The Fed eased three times, contributing to the overall fall for interest rates.

Asia's depression led to a halving of oil prices, and Asian needs for foreign exchange caused the dollar price of Asian manufactured goods to fall by 16 percent. What you ended up with was a plunge for fixed rate mortgages in the U.S. and a boom for housing. In addition, the falling energy and import prices took the CPI down to 1.6 percent with wages running at 4 percent. That gave us the best real wage increase we've seen in 30 years.

A boom for housing and surging real wages combined to create a domestic spending boom. In the U.S., we have a high proclivity for spending on imports. A spending boom, obviously, gave us a boom for consumer goods imports and so despite a world-wide sharp shrinkage in trade, we actually had an 11 percent gain in import volumes coming into the United States in 1998. Put that together with exports at nearly a crawl and you can see that we were in the midst of a substantial and rapidly rising U.S. trade deficit.

Again, it bears repeating that the U.S. domestic demand boom allowed global purveyors of goods and services to weather the collapse of Asian demand. The U.S. lending and spending rescue worked in simple terms.

For the globe in the year 2000, however, Asian recovery and moderating recessions in Latin America suggest that we'll have the best rest-of-world performance since 1996. From my perspective then, it's straightforward that the problem the U.S. faces, as we contemplate the trade deficit in the year 2000 and beyond is one of engineering a return to a Goldilocks U.S. real economy growth rate.

Simply put, the rest of world recovery doesn't allow for the kind of boom that we've had in 1998, 1999. If you look at the large and rapidly growing U.S. current account imbalance, in this context, it's the simplest measure that speaks to the long-run unsustainable trajectory of the U.S. economy.

I think a downshift for U.S. domestic spending is necessary to both contain the growth of U.S. international deficit and to return the U.S. to a sustainable growth trajectory.

If you think about the outsized U.S. external deficit in these terms, you have to think about macro dynamics. A desire to shrink the U.S. imbalance, therefore, requires U.S. policy makers to lobby for faster spending abroad and acquiesce to additional Fed tightening at home.

VICE CHAIRMAN PAPADIMITRIOU: Thank you very much. Professor Blinder?